24

Office-Supreme Court, U.
FILED
JUL 28 1951
CHARLES ELMORE CROPL
CLE

IN THE

Supreme Court of the United States

OCTOBER TERM, 1951

NO. 210

MRS. ODILE V. HUBERT TUCKER, AS A STOCKHOLDER, ON BEHALF OF CRESCENT CITY LAUNDRIES, INC.,
Petitioners,

vs.

NEW ORLEANS LAUNDRIES, INC., ET AL.,
Respondents.

Petition

William G. McRae,
Richard A. Dowling,
Attorneys for Petitioners.

TABLE OF CONTENTS

Page

Opinion Below 1

Jurisdiction 2

Statutes Involved 2

Questions Presented 3

Specification of Error to be Urged 3

Summary Statement 3

Reasons for Granting the Writ 5

Supporting Brief 8

I. THE WEIGHT OF FEDERAL DECISIONS WHICH HAVE DEALT WITH STOCKHOLDERS' DERIVATIVE ACTIONS TO ENFORCE A CORPORATION'S RIGHTS AGAINST ITS MAJORTY DIRECTORS FOR FRAUDULENT BREACHES OF TRUST TOWARD IT, HOLD:

(a) WITH RESPECT TO THE CONTROVERSY PRESENTED, THE CORPORATION IS ON ONE SIDE, AND THE WRONGDOERS ARE ON THE OTHER;

(b) THE CORPORATION MUST BE REALIGNED AS A COMPLAINANT FOR THE PURPOSE OF DETERMINING DIVERSITY JURISDICTION 8

A. This Court has not authorized an exception in stockholders' derivative action to the rule which

obligates Federal courts to realign parties for jurisdictional purposes according to their real interests . 11

B. The decisions of other lower Federal courts cited as authority did not authorize an exception, in stockholders' derivative action, to the rule which obligates Federal courts to realign parties for jurisdictional purposes according to their real interests 16

C. Decisions which have held that the general rule of realignment does not apply in stockholders' derivative actions, including the decision of the Court of Appeals in this case, are unsound, and in conflict with the decisions of this Court 19

D. The rule of undivided loyalty of agent to his principal forbids agent to be personally interested adversely to the rights of his principal. When that antagonism arises, the law terminates the agency. This rule is applicable to directors as agents of a corporation. This Court has not sanctioned a departure from this rule in stockholders' derivative actions 24

E. A corporation's position can not be fixed as having approved fraudulent breaches of trust by its directors, except upon an unanimous vote of its stockholders. Its directors can not ratify their fraud against the corporation on its behalf, where they do not own all of its stock 26

II. THE COMPLAINING STOCKHOLDER IN A STOCKHOLDERS' DERIVATIVE ACTION SHOULD BE REGARDED AS A NOMINAL PARTY WHOSE CITIZENSHIP IS IMMATERIAL IN DETERMINING DIVERSITY JURISDICTION . 27

III. THE POSITION OF AN INJURED CORPORATION IN A STOCKHOLDERS' DERIVATIVE ACTION CAN NOT BE FIXED AS THAT OF A REAL DEFENDANT BECAUSE IT IS IN THE ANTAGONISTIC HANDS OF THE MAJORITY DIRECTORS AND STOCKHOLDERS WHOSE FRAUD IS THE ESSENCE OF THE ACTION 30

Public Importance of The Issues 33

Conclusion 36

CASES CITED:

Anderson v. Gailey, 33 F. (2d) 589 25

Arapahoe County v. Kansas Pacific Ry Co., (1877) Fed. Cas. No. 502, 4 Dill. 277 . . . 9, 21, 30, 35

Bates Street Shirt Co. v. Waite (Me.) 156 A. 293 . . 26

Blumenthal v. Craig (CCA) 81 F. 320 28

Bush v. Elliott, 202 U.S. 477 . . . . . 6, 29

Camden Land Co v. Lewis, 101 Me. 78, 63 A. 523 . 25, 27

Chaplin v. Selznick, 293 N. Y. 529, 58 N. E. (2d) 719 . 28

Chaplin v. Selznick, 58 N.Y.S. (2d) 453 32

City of Indianapolis v. Chase National Bank, 314 U.S. 63 . . . . . 6, 15, 16

Commonwealth Finance Corp., v. McHarg, (CCA 2) 282 F. 569 24

Dana v. Morgan, 219 F. 313 27

De Neufville v. New York & Northern Ry. Co., (CCA 2) 81 F. 10 . . . . . 6, 14, 20, 34

Denike v. Anglo California Nat. Bank, (CCA 9) 145 F. (2d) 285 28

Doctor v. Harrington, 196
U.S. 579 . . 6, 10, 11, 12, 13, 14, 15, 16, 19, 22, 23

Dodge v. Woolsey, 59 U.S. 9, 18 How. 331 . . 10, 11, 20

East Tennesssee, etc. R. R. v. Grayson,
119 U.S. 240 . . . . . 20, 22, 23

Greenwood v. Freight Co., 105 U.S. 13 . . . 20, 21, 23

Groel v. United Electric Co., (CC, N.J., 1904)
132 F. 252 . . . . . 20, 21, 22

Hamer v. New York Railways Co.,
244 U.S. 266 . . . . . 7, 14, 15, 23

Harris v. Brown, (D.C. Ky.) 6 F (2d) 922 . . . 10, 17

Hawes v. Oakland, 104 U.S. 450 . . . . . 20, 22

Hodgeman v. Atlantic Ref. Co., 300 F. 590 27

J.R.A. Corporation v. Boylan, 30 F. Supp. 393, affirmed
on opinion below, (CCA 2) 109 F. (2d) 1018 . 10, 17

Johnson v. Brandon Corp., (CA 4) 183 F. (2d) 445 . 10

Kelly v. Queeney, (W.D. N.Y.) 41 F. Supp. 1015 . 10, 17

Klein v. Independent Brewing Ass'n., 231 Ill. 594,
83 N. E. 434 25

Kohler v. McClellan, (D.C. La.) 77 F Supp. 308 . . 28

Koster v. (American) Lumbermen's Mutual
Cacualty Co., 330 U.S. 518 . . 10, 13, 14, 19, 28

Lamb v. Parrott Silver & Copper Co.,
(CC, 1901) 112 F. 241 9

Laughner, et al. v. Schell, (CCA3) 260 F. 396 . . 7, 9, 34

Lavin v. Lavin, (CA 2) 182 F. (2d) 870 . . . 10, 18, 19

Lucas v. Millican, (CC, 190) 139 F. 816 9

Meeker v. Winthrop Iron Co., 17 F. 4[illegible] 27

Meyers v. Smith, 190 Minn. 157, 251 N.W. 20 . . . 31

Nagle v. Wyoga Gas & Oil Corp., (D.C. Pa.)
10 F. Supp. 905 . . . . . 10, 17

New Jersey Central R. Co. v. Mills,
113 U.S. 249 . . . . . 20, 21, 22, 23

Otis & Co., v. Pennsylvania R. Co., 57 F. Supp 680 . . 31

Pacific R. R. v. Ketchum, 101 U.S. 289 11

Removal Cases, 100 U.S. 457 11

Slutzker v. Reiber, 132 N.J. Eq. 412, 28 A. (2d) 258 . 31

Smallen v. Louisville Fire & Marine Ins. Co.,
(D.C. Ky.) 80 F. Supp. 279 . . . . . 10, 17

Stewart v. B. & O. Railroad Co., 168 U.S. 445 . . 6, 29

Stewart v. Dunham, 151 U.S. 61 18

Tachna v. Insuranshares Corp. of Delaware,
(D.C. Mass.) 25 F. Supp. 541 . . . . . 10, 18

Temmen v. Courtney, 1 S.W. 875, 8 Ky. L. 921 . . . 24

Venner v. Great Northern Ry. Co.,
209 U. S. 24 . . . . . 10, 14, 15, 16, 17, 23

Voss v. Neineber, 68 F. 947 28

Walden v. Skinner, 101 U.S. 577 30

Wardell v. Railroad Company, 103 U.S. 651 . . . 7, 27

Wood v. City National Bank & Trust Co., 312 U.S. 262 . 25

Zahn v. Transamerica Corp., (CCA 3) 162 F. (2d) 36 . 26

FEDERAL RULES OF CIVIL PROCEDURE:

Rule 23 (b) 14

Rule 82 14

STATUTES:

28 U.S.C., Section 1254(1) 2

28 U.S.C., Section 1332 . . . . . 2, 8, 9, 33

28 U.S.C., Section 1401 2

28 U.S.C., Section 1695 . . . . . 2, 3

Act of March 3, 1875, (18 Stst. part 3, 470) . . 11

11 U.S.C.A., Section 46 (b) 29

TEXT BOOKS:

Cook, Corporations, 8th. Ed. Section 730 . . . 27

Corpus Juris Secundum, Section 567, verbo Corporations, Vol. 18, p. 1288 29

Fletcher, CYC. of Corp., Sec. 5795 29

Pomeroy on Equity Jurisprudence, 4th Ed., 1095 . 28

U. S. CONSTITUTION:

Article III, Section 2 8

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1951

NO.....

MRS. ODILE V. HUBERT TUCKER, AS A STOCKHOLDER, ON BEHALF OF CRESCENT CITY LAUNDRIES, INC.,
Petitioners,

vs.

NEW ORLEANS LAUNDRIES, INC., ET AL.,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF

Now comes Mrs. Odile V. Hubert Tucker, as a stockholder on behalf of Crescent City Laundries, Inc., and prays that a writ of certiorari issue to the United States Court of Appeals for the Fifth Circuit, to review here the record and judgment entered by that court in the above action on April 5, 1951 (R.475).

OPINION BELOW.

The opinion of the Court of Appeals was rendered on April 5, 1951 (R.472) and is not yet reported. Petition for Rehearing was filed April 25, 1951 (R.476) and was denied May 10, 1951 (R.486). The opinion of the District Court is reported in 90 F. Supp. 290 and is found in (R.436).

JURISDICTION.

The jurisdiction of this Court is invoked under Section 1254(1), Title 28, United States Code.

STATUTES INVOLVED.

This action was brought by Mrs. Tucker, as a stockholder, solely on behalf of Crescent City Laundries, Inc., a Maine corporation. It seeks to enforce Crescent's claims against numerous defendants, including a majority of Crescent's directors and stockholders, all of whom are citizens of states other than Maine. Said claims arose out of fraudulent breaches of trust by said directors toward said corporation whereby its property was misappropriated to said directors and others who confederated with them. Jurisdiction is based upon the requisite statutory amount in controversy between citizens of different States under Section 1332, Title 28, United States Code, which provides:

> "Section 1332(a). The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $3000 exclusive of interest and costs, and is between: ***
>
> (3 Citizens of different States and in which foreign states or citizens or subjects thereof are additional parties."

This action was filed in the United States District Court for the Eastern District of Louisiana under Section 1401, Title 28, United States Code, which provides:

> "Section 1401. Any civil action by a stockholder on behalf of his corporation may be prosecuted in any judicial district where the corporation might have sued the same defendants."

Extraterritorial services of process upon Crescent was made on Ernest L. McLean, Clerk of Crescent, at Augusta, Maine, under Section 1695, Title 28, United States Code, which provides:

"Section 1695. Process in a stockholder's action in behalf of his corporation may be served upon such corporation in any district where it is organized or licensed to do business or is doing business."

QUESTIONS PRESENTED

1. Are Federal courts obligated to realign the parties for jurisdictional purposes, according to their real interests in the controversy in a stockholders' derivative action, to enforce their corporation's rights against its majority directors for fraudulent breaches of trust toward it in misappropriating its assets to themselves?

2. If the injured corporation, in such an action, must be realigned as a complainant, then is the complaining stockholder to be regarded only as a formal or nominal party whose individual citizenship is immaterial in determining diversity jurisdiction?

3. May the position of the injured corporation, in such action, be fixed as a defendant because it is in antagonistic hands, where fraud of the majority directors and stockholders is the essence of the stockholders' derivative action?

SPECIFICATION OF ERRORS

The Court of Appeals erred in affirming the judgment of the District Court dismissing this action upon the ground that diversity of citizenship between the parties to the controversy, as stated in the complaint, is lacking.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

Mrs. Tucker, as a preferred stockholder, instituted this stockholders' derivative action on behalf of her corporation, Crescent City Laundries, Inc., a citizen of the State of Maine. More than $3000, exclusive of interest and costs, is in dispute. Mrs. Tucker is a citizen of the State of Louisiana.

Named as defendants are Crescent, a nominal defendant, and numerous real defendants, including a majority of Crescent's directors and stockholders or their personal representatives, many of whom are citizens of the same state as Mrs. Tucker. The complaint asserts Crescent's claims against said directors for fraudulent breaches of trust to it, whereby its entire assets were misappropriated by said directors to themselves and others confederated with them. The relief demanded is the impressing of a constructive trust upon certain of said assets in favor of the corporation, and an accounting to the corporation as well as a personal judgment in favor of Crescent against certain defendants for the damages sustained by the corporation as a result of the breaches of trust alleged. The directors of Crescent abandoned their duties to it in 1942, and thereafter Crescent was disabled from continuing its regular business as a result of the acts complained of. (R. 171-210).

Jurisdiction is invoked upon the ground of requisite amount in controversy and diversity of citizenship between the parties to the controversy, i.e., Crescent, a citizen of Maine, on one side, and the other defendants, all of whom are citizens of other states, on the other.

All of the defendants, except Crescent, moved to dismiss for lack of jurisdiction, for want of the requisite diversity of citizenship between the parties to the dispute. Crescent filed no responsive pleadings. The District Court concluded that the controversy was between the plaintiff stockholder, on one side, and Crescent and the alleged wrongdoers on the other (R. 440, 441), and that the requisite diversity was lacking, and ordered the action dismissed. (R. 451) Upon appeal the Court of Appeals for the Fifth Circuit affirmed the judgment of the District Court. (R. 475).

REASONS FOR GRANTING THE WRIT.

This case presents important new questions with respect to the diversity jurisdiction of the Federal courts, depending upon the proper realignment and classification of the parties in a stockholders' derivative action which asserts the injured corporation's demands against its majority directors for their fraudulent breaches of trust toward their corporation, *in instances where the injured corporation and its wrongdoing directors are citizens of different states.*

The decision of the Court of Appeals should be reveiwed because:

1. This Court has never decided the question of the proper realignment and classification of the parties for the purpose of determining diversity jurisdiction in a stockholders' bill where the only demand was for a recovery for the corporation against the majority corporate directors for fraudulent breaches of trust in the misappropriation of the corporation's assets to themselves.

2. It is essential to the due administration of justice, and to the jurisdictional integrity of the Federal courts, that the rule obligating Federal courts to realign the parties for jurisdictional purposes according to their real interests in the controversy be strictly adhered to by the lower Federal courts in all civil actions.

3. It is a matter of public importance that the public policy of requiring the faithful discharge of duties by persons holding positions of trust and confidence be rigidly enforced. This Court should decide whether or not majority directors who are guilty of fraudulent breaches of trust to their corporation are disqualified, by reason of their interests being adverse to the interest of their corporation, from determining the attitude of the corporation in a stockholders' derivative action against said directors, seeking to redress such fraudulent breaches of trust.

4. Such a decision by this Court will have immediate importance far beyond the particular facts and parties involved in this case.

5. The decision of the Court of Appeals misinterpreted the decision of this Court in *Doctor v. Harrington, 196 U.S. 579,* in construing that case as holding that, for the purpose of determining diversity jurisdiction of a stockholders' derivitive action, the court is not required to realign the parties according to their real interests in the controversy because the corporation is in antagonistic hands.

6. The decision of the Court of Appeals is in conflict with the decision of this Court in *City of Indianapolis v. Chase National Bank, 314 U.S. 63,* which holds that it is the duty of Federal courts in civil actions to look beyond the pleadings and arrange the parties according to their sides in the dispute, as shown by the facts stated in the complaint.

7. The decision of the Court of Appeals is in conflict with the decision of this Court in *Stewart v. B. & O. Railroad Co., 168 U.S. 445,* which holds that for the purpose of determining diversity jurisdiction in the Federal courts in an action brought for another's benefit, regard is had to the citizenship of the real rather than the nominal plaintiff.

8. The decision of the Court of Appeals is in conflict with the decision of this Court in *Bush v. Elliott, 202 U.S. 477,* which holds that, where a person having a derivative right to enforce another's cause of action on behalf of such other person, it is the citizenship of the person whose cause of action is sought to be enforced that controls in determining the question of diversity of citizenship jurisdiction.

9. The decision of the Court of Appeals is in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *De Neufville v. New York & Northern Ry. Co., 81 F. 10,* and with the decision of the Circuit Court of Appeals

for the Third Circuit in *Laughner, et al., v. Schell, 260 F. 396,* which hold that the controversy in a stockholders' derivative action against wrongdoing directors is one between the injured corporation, on one side, and its wrongdoing directors on the other.

10. The decision of the Court of Appeals is in conflict with the decision of *Laughner v. Schell, supra,* which holds that the injured corporation should be realigned as complainant in a stockholders' derivative action to enforce its claim against its wrongdoing directors.

11. The decision of the Court of Appeals is contrary to the decision of this Court in *Hamer v. New York Railways Co., 244 U.S. 266,* which holds that the real party in interest in a derivative action brought on its behalf should be realigned as a complainant, where it is not made an adversary, to be classed for purposes of jurisdiction with the real defendants, and does not in effect range itself in opposition to the relief sought.

12. The decision of the Court of Appeals is in conflict with the decision of this Court in *Wardell v. Railroad Company, 103 U.S. 651,* which holds that directors of a corporation can not, with respect to the same matters, act for themselves and for the corporation.

13. This is the first occasion that there has been presented to this court for decision the question as to whether or not the injured corporation, in a stockholders' derivative action to enforce its rights against its majority directors arising out of their fraudulent breaches of trust toward it, may take a position which is fundamentally antagonistic to the claims asserted on its behalf.

14. The decision of the Court of Appeals has decided important questions of federal law which have not been, but should be, settled by this Court.

SUPPORTING BRIEF

I.

THE WEIGHT OF AUTHORITY OF FEDERAL DECISIONS WHICH HAVE DEALT WITH STOCKHOLDERS' DERIVATIVE ACTIONS TO ENFORCE A CORPORATION'S RIGHTS AGAINST ITS MAJORITY DIRECTORS FOR FRAUDULENT BREACHES OF TRUST TOWARD IT, HOLD:

(a) WITH RESPECT TO THE CONTROVERSY PRESENTED, THE CORPORATION IS ON ONE SIDE, AND THE WRONGDOERS ARE ON THE OTHER;

(b) THE CORPORATION MUST BE REALIGNED AS A COMPLAINANT FOR THE PURPOSE OF DETERMINING DIVERSITY JURISDICTION.

The complaint in this stockholders' derivative action seeks to do exactly what the corporation itself might have done had it been free and competent to act for itself, i.e., to enforce the corporation's causes of action against its majority directors who conspired among themselves and with third persons to defraud it, in violation of their fiduciary duties to it. The complaining stockholder does not state any individual cause of action against her corporation or any defendant, nor does she seek individual relief against any of them.

Jurisdiction is invoked upon the ground of the amount involved and the diversity of citizenship existing between the parties to the controversy.

Jurisdiction is conferred upon federal courts by the *Constitution, Art. III, Section 2,* and upon district courts by Congress in *Section 1332, Title 28, U.S.C.*, "of *controversies* between citizens of different States."

Where, as here, the complaint in a civil action filed in a district court presents a matter in controversy which exceeds

the value stated in *Section 1332, supra,* and which is between citizens of different States, the district court has jurisdiction. Other parties being upon the record does not defeat jurisdiction in such case. There is no mention of "plaintiff" or "defendant" in the statute conferring diversity jurisdiction upon district courts. The actual parties to the dispute in this action are Crescent, a citizen of Maine, on one side, and those whose acts are complained of, all whom are citizens of states other than Maine, on the other; — hence, diversity exists between the parties to the controversy.

The two lower courts concurred in the view that such a controversy, when presented to the court through the medium of a stockholders' derivative action, is converted into one between the complaining stockholder, on one side, and the injured corporation and its wrongdoers on the other, because the corporation is in antagonistic hands. (R440).

The weight of Federal decisions, in such cases, holds that the injured corporation must be realigned as a complainant, where its interest lies:

> *Arapahoe County v. Kansas Pacific Ry. Co., (1877), Fed. Cas. No. 502, 4 Dill. 277,* (Opinion by Mr. Justice Miller of the Supreme Court, sitting in Circuit); *Lamb v. Parrott Silver & Copper Co., (CC, 1901), 112 Fed. 241; Lucas v. Millican, (CC, 1905), 139 Fed. 816;* and *Laughner v. Schell, (CCA3, 1919), 260 Fed. 396.*

A stockholders' bill, naming their corporation as a defendant, may be brought solely in the rights of the stockholders; or, solely in the right of their corporation; or such bill may combine a right of action existing in themselves against their corporation and others with a right of action existing in their corporation against third persons. When brought *solely* in the right of the corporation it is a stockholders' derivative action. The rule for determining the diversity jurisdiction of federal

courts in each type of bill is different. *Johnson v. Brandon Corp., (CA 4) 183 F. (2d) 445.*

Petitioners earnestly urge that where the stockholders' bill, as here, declares only upon their corporation's right of action against other defendants, including a majority of its directors who are guilty of fraudulent breaches of trust toward their corporation, and the corporation's interest is in no way adverse to the success of the action, the corporation must be realigned as a complainant. The right of action thus declared upon is entirely derivative.

The basis of the decisions of the two lower courts in this case was;—that it was not the duty of Federal courts to realign the injured corporation in such cases because it was in antagonistic hands. Cited as controlling authority for this view are

> *Dodge v. Woolsey, 59 U.S. 9, 18 How. 331; Doctor v. Harrington, 196 U.S. 579; Venner v. Great Northern Railway, 209 U.S. 24; Koster v. Lumbermen's Mutual Casualty Co., 330 U.S. 518; Harris v. Brown, et al., 6 F. (2d) 922; Nagle v. Wyoga Gas & Oil Corp., et al., 10 F. Supp. 905; Kelly v. Queeney, 41 F. Supp. 1015; Smallen v. Louisville Fire & Marine Insurance Co., 80 F. Supp. 279; J.R.A. Corporation v. Boylan, et al., 30 F. Supp. 393,* affirmed on opinion below, *109 F. (2d) 1018; Tachna v. Insuranshares Corporation of Delaware, 25 F. Supp. 541,* and *Lavin v. Lavin, 182 F. (2d) 870.*

Petitioners contend that none of the decisions so cited, when consideration is had for the facts in each case and the law as applied thereto, authorize federal courts to refuse to realign the injured corporation as a complainant in a stockholders' derivative action because it is in antagonistic hands—when its interest is not adverse to the success of the action.

A.

This Court has not authorized an exception in stockholders' derivative action to the rule which obligates Federal Courts to realign parties for jurisdictional purposes according to their real interests.

Dodge v. Woolsey, supra, is said by the District Court (R. 440) to be the leading case upon the question of the refusal of the courts to realign the corporate defendant in whose behalf plaintiff sues, as a party plaintiff. That case was decided in 1855, which was twenty years before the passage of the Act of March 3, 1875, (18 Stat., part 3,470). This Court, in the *Removal Cases, 100 U.S. 457,* held that Act to require the realignment of parties in removal cases for the purpose of determining diversity jurisdiction. In *Pacific R. R. v. Ketchum, 101 U.S. 289,* this Court held said Act also required such realignment in other cases. *Dodge v. Woolsey, supra,* does not, therefore, furnish support for the decision of the Court of Appeals in this case, because the statute requiring realignment could not have been anticipated when *Dodge v. Woolsey, supra,* was decided.

Contrary to the misinterpretation placed by the lower courts upon the decision of this Court in *Doctor v. Harrington, supra,* that case was *not* a stockholders' derivative action. The two stockholders in that case sued *in their own rights,* and *not exclusively in the right of their corporation,* the Sol Sayles Company. This misinterpretation has doubtless been due to the fact that the opinion of this Court did not fully disclose all the allegations of the complaint and the relief which was sought. Such misinterpretation is also the result of the tendency of the lower courts to give undeserved weight to the words:

> "but the corporation may be under a control antagonistic to him, and made to act in a way detrimental to his rights."

Antagonistic control of the corporation is at the root of every stockholders' bill against his corporation;—both when he sues it to enforce a right of his own against it, as well as where he makes it a nominal defendant, in a derivative action, to enforce its cause of action against others.

In attaching unwarranted significance to the above quoted language of the opinion, the lower courts have disregarded the language of this Court which was the real basis of its decision in *Doctor v. Harrington, supra,* to-wit:

> "If a controversy hence arises, and the other conditions of jurisdiction exist, it can be litigated in a Federal court."

The only basis upon which this Court could have upheld diversity jurisdiction in *Doctor v. Harrington, supra,* was that a controversy involving the requisite amount actually existed between the complaining stockholders, who were citizens of New Jersey, and their corporation and the other defendants, all of whom were citizens of New York;—hence, one between citizens of different states. This was the basis of its decision. Its refusal to realign the corporation as complainant was because the stockholders were suing to enforce their personal rights against it. *The principal purpose of the suit was to divest the Sol Sayles Company, of which complainants were stockholders, of its title to all of its property and to vest the title thereto in complainants and its other stockholders.* Complainants sought an accounting from the corporation and the distribution to its stockholders of—all of its property; and further sought to recover from certain directors specific property in their hands which it was claimed belonged to the corporation, the latter, if recovered, to be distributed to all stockholders along with the other assets of

the corporation. As it appears of file in this Court, the Eighth, Twelfth and Twenty-second paragraphs, together with the demands for relief in the complaint, clearly show:

(1) That the stockholder-complainants demanded an accounting from their corporation, the Sol Sayles Company, and that all of its property when accounted for be distributed to its stockholders.

(2) That the corporation's property consisted of accounts, bills receivable and other assets of great value due the corporation direct and in addition, the assets sought to be recovered for the benefit of the corporation from its directors.

(3) That the granting of the relief prayed for against their corporation would have stripped it of all of its assets—and left it an empty shell.

Clearly—then, *Doctor v. Harrington, supra,* cannot be regarded as authority for sanctioning the refusal of a federal court to realign the injured corporation in a stockholders' derivative action as a complainant because it is in antagonistic hands, where, as here, the injured corporation's interest is not in any way adverse to the success of the action.

The reference to *Doctor v. Harrington, supra,* in *Koster v. Lumbermen's, supra,* does not change the law as it was actually applied and intended to apply in the former case. The only question presented to this Court for decision in the *Koster Case, supra,* was the application of the doctrine of *forum non conveniens* in a derivative action. The issue was raised by the *injured corporation.* It was the only question decided in the majority opinion.

In one of the dissenting opinions in *Koster v. Lumbermen's, supra,* Mr. Justice Reed, concurred in by Mr. Justice Burton—on page 534 of 330 U.S., said:

> "We need not tarry to consider the small interest of the plaintiff in the assets of his corporation, nor the effect of realigning the corporation on the side of the cause where its true interest lies. However interesting the implications of these facts, they have nothing to do with a dismissal on the ground of the inconvenience of the forum. The same facts would exist no matter what the forum, and they are accordingly not pertinent to our inquiry."

It is unmistakable from the foregoing that this Court, as a whole, was not concerned with the doctrine of the realignment of parties in derivative actions in *Koster v. Lumbermen's, supra,* and that it gave no serious consideration to the basis of its ruling in *Doctor v. Harrington, supra.*

The only other case to come before this Court after *Doctor v. Harrington, supra,* where the question presented and decided, was the realignment of parties in a stockholders' bill is the case of *Venner v. Great Northern Ry. Co., 209 U.S. 24,* decided in 1908. This Court held:

> "in an action against the corporation and others by one of the stockholders, that where the complaint alleges *joint* fraudulent conduct on the part of the corporation and other defendants with whom it *jointly* resists that charge, the corporation cannot be realigned as a party plaintiff even if it might be to its financial interest to have plaintiff prevail." (Emphasis supplied)

Venner v. Great Northern, supra, also decided, adversely to *De Neufville v. New York & Northern Ry. Co.,* 81 *F.* 10, that equity rule 94 does not affect Federal jurisdiction. Rule 23(b) of the Federal Rules of Civil Procedure is the successor to equity rule 94. Rule 82 F.R.C.P. expressly provides:

> "These rules shall not be construed to extend or limit the jurisdiction of the district courts of the United States or the venue of actions therein."

In *Hamer v. New York Railways Co., (1917), 244 U.S. 266,* a case involving the proper realignment of a trustee

made defendant in a suit brought by beneficiaries in the right of the trustee, upon the refusal of the trustee to sue, this Court said at page 274:

> "It is not contended that this refusal to sue makes the Trust Company an adversary, to be classed for purposes of jurisdiction with the real defendants,—as in those cases where the refusal to sue was part of a fraudulent participation in the wrongdoing, and where the trustee or corporation in effect ranged itself in opposition to the relief sought.[3] The Trust Company having, as we have shown, a real interest in the controversy, which makes it a necessary party to the suit, must be aligned as a party plaintiff, where its interest lies.[4]"
>
> * * * * *
>
> "3. Venner v. Gt. N. R. Co., 209 U.S. 24; Doc. v. Harrington, 196 U.S. 579; Kelly v. River Coaling Co., 172 Fed. 482; Groel v. United El. Co., 132 Fed. 252.
>
> "4. Blalock v. Small, 127 U.S. 96; Harter v. Kernochen, 103 U.S. 562; Pac. R. Co. v. Ketchum, 101 U.S. 289; Allen-West Commission Co. v. Brashear, 176 Fed. 110; Shipp v. Williams, 10 CCA 247."
>
> * * * * *

It appears that this Court, in the *Hamer Case, supra,* apparently considered the rule as to realignment of parties to be the same in actions by stockholders on behalf of their corporations, as in actions by beneficiaries in the right of trustees, and not different from the rule in other civil actions. That is, for purposes of determining diversity jurisdiction the parties must be realigned according to their real interests in the controversy.

There has been no decision of this Court since the *Hamer Case, supra,* in which the question of the realignment of parties in derivative actions has been directly presented and decided.

In *City of Indianapolis v. Chase National Bank, supra,* at pages 69 and 70 of 314 U.S., this Court said:

> "It is our duty, as it is that of the lower federal courts, to 'look beyond the pleadings and arrange the parties according to their sides in the dispute.' *** Litigation is the pursuit of practical ends not a game of chess. *** Whether the necessary 'collision of interest' exists is therefore not to be determined by mechanical rules. It must be ascertained from the 'principal purpose of the suit' and the 'primary and controlling matter in dispute.' These familiar doctrines governing the alignment of parties for purposes of determining diversity of citizenship have consistently guided the lower federal courts and this court."

Doctor v. Harrington, supra, and Venner v. Great N. R. Co., supra, were cited in support of the doctrine so announced, without qualification.

There is no conflict between the majority and minority opinions of this Court upon the doctrine of realignment, as applied to a nominal defendant, which was precisely stated in the minority opinion in *Indianapolis v. Chase, supra, at page 80 of 314 U.S.*, as follows:

> "The doctrine of realignment permits and requires a nominal defendant to be treated as a plaintiff for the purpose of defining the real controversy where no real cause of action is asserted against him by the plaintiff, but it does not admit of such treatment of a defendant against whom the plaintiff asserts a cause of action within the jurisdiction of the court."

B.

The decisions of other lower Federal Courts cited as authority did not authorize an exception, in stockholders' derivative action, to the rule which obligates Federal Courts to realign parties for jurisdictional purposes according to their real interests.

The following decisions—cited in the opinion of the District Court—as sustaining an exception to the rule of re-

alignment, in stockholders' derivative actions, are not in point:

The court, speaking of the rule of realignment in *Harris v. Brown, supra,* at page 924, said:

> "This rule, however, has never been invoked in stockholders' bills; if so, it would be impossible for a non-resident stockholder to ever bring a stockholders' bill in the federal court, no matter how flagrantly the officers of the company were violating their duty to the corporation and its stockholders."

The stockholder was suing in his own right to enjoin certain persons from acting as directors of his corporation. Hence, the ruling had no application in a stockholders' derivative action.

Nagle v. Wyoga Oil & Gas Corp., supra, was a case where the plaintiff stockholders were parties to the controversy in their own right. They sought the appointment of a receiver for their corporation.

Kelly v. Queeney, supra, was not a stockholders' bill, and no ruling in that case is applicable in this action.

In *Smallen v. Louisville Fire & Marine Insurance Co., supra,* the refusal to realign the corporation as a complainant was based upon the decision of this Court in *Venner v. Great Northern Ry. Co., supra,* in that, the corporation and the directors were alleged to have engaged in the same illegal and fraudulent conduct, and the injury was alleged to have been accomplished by their joint action.

J.R.A. Corporation v. Boylan, supra, was an action brought in the personal right of the stockholders. The corporation, The American Tobacco Company, was charged with violating its charter and by-laws in adopting illegal stock purchase and bonus plans, which the stockholder, suing in his own right, claimed to be entitled to have set aside.

Tachna v. Insuranshares Corp., supra, is not authority for the exception invoked. This point was not before the court for decision. The only question before the court in that case was an application of Massachusetts stockholders to intervene. The court had original jurisdiction of the case as it stood—which could not have been ousted because of the citizenship of persons whom the court might permit to intervene as held in *Stewart v. Dunham, 151 U.S. 61.* What the court said, in speculating as to what its jurisdiction might have been—had the suit been otherwise brought, was pure obiter dicta.

Lavin v. Lavin, supra, cited by the Court of Appeals, does not sustain the exception. The facts set forth in the *Lavin Case, supra,* do not show the nature of the allegations made against the corporation and the relief demanded against it. However, the record in the case in the Court of Appeals for the Second Circuit—discloses that the non-derivative relief demanded against the stockholder's corporation by the stockholder was as follows:

> "(2) cancellation of a burdensome management agreement imposed by the individual defendants upon the corporation (fols. 25-38);
>
> (6) cancellation of an improvident and burdensome long-term lease made by the corporation in fraud of plaintiff's rights and in violation of Sec. 20 of the Stock Corporation Law (fols. 64-73);
>
> (7) appointment of a receiver for Sanford Hotel Corporation to bring suit to cancel and set aside leases and agreements referred to in (6); and
>
> (8) that defendants be required to declare and pay dividends on plaintiff's shares of stock. (fol. 78)"

In his opinion in the *Lavin Case, supra,* Chief Judge Learned Hand said:

> "It may indeed be doubted whether as an original question the Supreme Court would not today align the corporation as a party plaintiff in all cases;[3] nevertheless

it has shown no disposition to change the rule in Doctor v. Harrington 196 U.S. 579, 25 S.Ct. 355, 49 L. Ed. 606, but has recognized its continuing authority."

* * * * *

"3. Koster v. American Lumbermen's Mutual Casualty Co., 330 U.S. 518, 522, 533, 67 S. Ct. 828, 91 L. Ed. 1067."

* * * * *

The plaintiff stockholder and his corporation were both citizens of the State of New York in the *Lavin Case, supra.* The stockholder having alleged an individual cause of action against his corporation and demanded relief against it, thereby making it an adversary, the court properly held that there was a lack of diversity jurisdiction.

The cases cited by the lower courts are authority only for the proposition that, where a stockholder's bill alleges an individual cause of action against his corporation and demands relief against it, the corporation must be treated as a real defendant. None of them are authority for the proposition that the corporation, made a nominal defendant in a stockholders' derivative action, shall not be realigned as a complainant when its interest is not adverse to the success of the action.

C.

Decisions which have held that the general rule of realignment does not apply in stockholders' derivative actions, including the decision of the Court of Appeals in this case, are unsound, and in conflict with the decisions of this Court.

A review of the decisions of lower federal courts, which have held that the general rule of realignment is inapplicable in stockholders' derivative actions, shows that the reasons assigned for such holdings have been immature reflections,

and wholy untenable, in addition to being in conflict with the principles of law and equity, and contrary to the decisions of this Court.

De Neufville v. New York & Northern Ry. Co., supra, was a stockholders' derivative action apparently similar to this one. The court held that the real controversy was *between the corporation and those who deprived it of its property,* but, also held that the corporation could *not* be realigned as complainant because, as it said at page 13:

> "the decisions in Dodge v. Woolsey, 18 How. 331, Hawes v. Oakland, supra, (104 U.S. 450), and Quincy v. Steel, 120 U.S. 271, 7 S.Ct., 520, and the ninety-fourth rule in equity, seem to preclude a strict application, in cases such as the one at bar, of the rule that parties may be rearranged according to interest in the controversy." (Parenthesis ours)

Groel v. United Electric Co., (CC N.J., 1904), 132 F. 252 was a stockholders' derivative action similar to this one. In that case, at pages 261 and 262, the court, in our opinion, clearly demonstrated the fallacy of the reasons stated by the Circuit Court of Appeals in the *De Neufville Case, supra,* for refusing to realign the injured corporation as complainant in that case. However, after reviewing many authorities, including the decisions of this Court in *Greenwood v. Freight Co., 105 U.S. 13, New Jersey Central R. Co., v. Mills, 113 U.S. 249,* and *East Tennessee, etc., R. R. v. Grayson, 119 U.S. 240,* the court announced its view at pages 263 and 264 as follows:

> "The rule deduced from them is that, in a suit in equity instituted by a stockholder in his own name, but upon a right of action existing in his corporation, the stockholder's corporation will be aligned with the defendants whenever the officers or persons controlling the corporation are opposed to the object sought by the complaining stockholder, and that, when such opposition

> does not appear, the stockholder's corporation will be aligned with the complainants in the case. It may not be easy to bring the Arapahoe County Case and a few others into line with this rule. But it is believed that the cases decided by the Supreme Court involving the duty of classifying parties for the purpose of determining the question of the jurisdiction of the Circuit Courts of the United States have established this rule."

Petitioners contend that nothing contained in the three preceding cases cited from this Court authorized such a deduction. The lower court in the *Groel Case, supra,* must have thought that this Court had held the corporation to be a real defendant in each of these three cases because, as it stated at page 262, these three decisions supported the principle that:

> "as a corporation can act only through its authorized agents, the position assumed in a controversy by such agents must necessarily fix the position of the corporation."

It does not appear that the principle announced was in the minds of the Supreme Court when it decided either of these three cases, or that such cases authorize the application of the stated principle to the facts of this case.

The defect in the court's deduction in *Groel v. United El. Co., supra,* is that it entirely overlooked the fact that not a single one of the three cases here decided dealt with a stockholders' derivative action. Each was brought in the right of the suing stockholder, and not in the right of his corporation. In *Greenwood v. Freight Co., supra,* the stockholder sought an injunction against his corporation to prevent it from complying with a statute claimed to be unconstitutional. The corporation was a real defendant against whom relief was sought. In *New Jersey Central R. Co., v. Mills, supra,* the stockholder's corporation *united with other defendants* in defending the acts complained of, and in denying the charges of illegality and fraud made against all the defendants, and sought

to uphold a lease, to which it was a party, and which the stockholder sought to have adjudged invalid. Again the stockholder was suing in his own right and not in the right of his corporation. In *East Tennessee, etc., R.R. v. Grayson, supra,* the allegations of the bill were said by this Court to be to the effect that the stockholder's corporation was acting in harmony with another corporation to uphold the validity of a lease which was sought to be cancelled, and this court said that these allegations of the bill were the equivalent of the *joint answer* in *New Jersey Cen. R. Co. v. Mills, supra,* for the purpose of fixing the position of the corporation as a real defendant. In *East Tennessee, etc., R.R. v. Grayson, supra,* this Court said, at page 244 of 119 U.S.:

> "The principal purpose of the suit is to set aside the lease for want of authority to make it. For that purpose both the lessor and lessee are necessary parties. *Grayson is not suing for the Memphis & Charleston Company but for himself.* It is true a decree in his favor may be for the advantage of the Memphis & Charleston Company, but he does not represent the company in its corporate capacity, and has no authority to do so." (Emphasis supplied)

It thus seems clear that the reasons which were assigned by the court in *Groel v. United Electric Co., supra,* for its refusal to realign the injured corporation as complainant in that stockholders' derivative action, had no support in the cited decisions of this Court.

Doctor v. Harrington, supra, was next decided in 1905—and the exception is now sought to be justified, because the corporation is in antagonistic hands. Petitioners submit that this fact does not create a controversy between the stockholder and his corporation, or between the stockholder and those who wronged his corporation.

In *Hawes v. Oakland,* supra, this Court said a cause of action arose in favor of the stockholder against his corpo-

ration, where he made a demand upon it to sue *outsiders* upon a cause of action existing in its favor, and it refused to do so. This Court has never held that a cause of action arose in favor of the stockholder against his corporation or against its wrongdoers, where the stockholder made no demand upon the corporation to sue its majority directors for fraudulent breaches of trust to it.

The facts in this case, with respect to a demand upon the corporation to sue, are distinguishable from those in *Doctor v. Harrington, supra,* and *Venner v. Great Northern Ry. Co., supra.* Here no demand was made because it would have been futile. (R. 222). There was no refusal on the part of Crescent to sue in this case which could be deemed a fraudulent participation in the wrongdoing, as this Court, in *Hamer v. New York Railways Co., supra,* characterized the refusal of the corporation to sue in *Doctor v. Harrington, supra,* and *Venner v. Great Northern Ry Co., supra.*

This case is further distinguishable from the two last cited cases, in that, the cause of action declared upon here is one upon which Crescent itself might have sued the other defendants in a federal court, diversity existing between them; whereas, the cause of action in favor of the corporation in each of the other cases could not have been prosecuted by the corporation in the federal courts because the corporation and its wrongdoers were citizens of the same State. The federal courts assumed jurisdiction in *Doctor v. Harrington, supra,* and *Venner v. Great Northern Ry. Co., supra,* because the complaint in each of these cases stated an individual cause of action between the stockholder and his corporation, and they were citizens of different States.

D.

The rule of undivided loyalty of agent to principal forbids agent to be personally interested adversely to the rights of his principal. When that antagonism arises, the law terminates the agency. This rule is applicable to directors as agents of a corporation. This Court has not sanctioned a departure from this rule in stockholders' derivative actions.

In *Temmen v. Courtney, 1 S.W. 875, 877, 8 Ky. L. 921,* cited in *3 Corpus Juris Secundum, p. 138, Verbo Agency,* it is said:

> "An agent, whether general or special, must be faithful and disinterested in the management of his principal's business. He must not be personally interested adversely to the rights of his principal. 'When that antagonism arises, the law terminates the agency.' "

This salutary principle, so well stated, has been held to apply to officers and directors of corporations, who are regarded in courts of equity as trustees, where they purport to act as agents for their corporation in the sale of its assets and sell to themselves to its injury. *Commonwealth Finance Corp. v. McHarg, (CCA2) 282 F. 569.*

Such are the facts in this case as stated in the bill of complaint. (R. 21-97).

From the moment when each of Crescent's majority directors joined in the fraudulent conspiracy to divert to themselves assets used by it in its linen supply business, an antagonism arose between said agents and their principal. This principle of law vacated the directorship agencies with respect to their representation of the corporation in dealing with the corporation's claims for the recovery of those assets. Had the question of the advisability of bringing suit against

said directors been presented at a meeting of the Board of Directors, each of said majority directors would have been disqualified from voting on the question, *Anderson v. Gailey, 33 F. (2d) 589,* citing *10 Cyc. 790.* Nor could a majority of the stockholders have ratified their acts after this action was instituted. *Klein v. Independent Brewing Ass'n., 231 Ill. 594, 83 N.E. 434, 451.*

These majority directors have remained in office and they and their confederates continuously controlled a majority of the corporation's stock. They are disqualified to represent the corporation in the negotiation of a settlement of, or in the litigation of, its claims against themselves. Their personal antagonism to a demand that they account to the corporation in this stockholders' derivative action, should not fix the corporation's position as being unfriendly to the enforcement of the claims asserted on its behalf herein. Such antagonism is dictated by their own personal interests, rather than being impelled by the discharge of their duty of undivided loyalty to their principal. *Camden Land Co. v. Lewis, 101 Me. 78, 63 A. 523, 534.*

In *Wood v. City National Bank & Trust Co., 312 U.S. 262, 269,* this Court approved the principle stated by Judge Cardozo, later Justice of this Court, as set out in *Meinhard v. Salmon, 249 N.Y. 458, 465,* where he said:

> "Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions. *** Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not be consciously lowered by this court."

This Court, as we have shown, has not yet consciously sanctioned the "disintegrating erosion" of the exception to the rule of realignment invoked by the District Court and sanc-

tioned by the Court of Appeals in this case, and petitioners urge that this Court now disavow the holding of the Court of Appeals to the contrary.

E.

A corporation's position can not be fixed as having approved fraudulent breaches of trust by its directors, except upon an unanimous vote of its stockholders. Its directors can not ratify their fraud against the corporation on its behalf, where they do not own all of its stock.

It would be an absurd paradox in the name of equity and justice, to permit the status of a corporation, having claims against its unfaithful directors for fraudulent breaches of trust toward it, to be fixed by the antagonistic attitude of the same directors who betrayed their fiduciary duties to it—in subservience to their individual interests.

Crescent, being a corporation of the State of Maine, the laws of the State of Maine govern the relationship between the corporation and its directors and stockholders. *Zahn v. Transamerica Corporation (CCA 3) 162 F. (2d) 36 (3).*

The Supreme Court of the State of Maine, in Bates *Street Shirt Co. v. Waite, (Me.) 156 Atl. 293, 297,* said:

> "Directors have no authority to act for the corporation in matters in which they are personally interested. They owe their whole duty to the corporation, and they are not to be permitted to act when duty conflicts with interest. They cannot serve themselves and the corporation at the same time. European & N.A. Ry. Co. v. Poor, 59 Me. 277."

The decision of the Court of Appeals, in sanctioning the doctrine that the rule of realignment is inapplicable in a stockholders' derivative action—under the facts in this case, places the corporation in a position in which the law does not permit it to be placed; and also in a position in which, if the

majority of the directors and stockholders had attempted to place it, thereby attempting to ratify their acts on behalf of the corporation, a court of equity would have denounced their action as a wanton or fraudulent destruction of the rights of the minority stockholders and the corporation. *Camden Land Co. v. Lewis, supra.*

As said by the court in *Dana v. Morgan, 219 F. 313, 315:*

> "Fraud is incapable of condonation even by the largest majority of shareholders, short of universal concurrence."

To the same effect: *Meeker v. Winthrop Iron Co., 17 F. 48; Hodgman v. Atlantic Ref. Co., 300 F. 590, 599; Cook, Corporations, 8th Ed. Sec. 730; Fletcher, CYC. of Corp., Sec. 5795.*

The courts can not, in the name of equity and justice, presume that a corporation occupies a position with respect to a controversy, which the law, the principles of equity, and public policy, all forbid it to occupy.

This Court, in *Wardell v. Railroad Company, 103 U.S. 651,* held:

> "The directors of a corporation are subject to the obligations which the law imposes upon trustees and agents. They cannot, therefore, with respect to the same matters, act for themselves and for it, nor occupy a position in conflict with its interests."

That decision has been many times cited, universally followed, and never overruled.

II.

THE COMPLAINING STOCKHOLDER IN A STOCKHOLDER'S DERIVATIVE ACTION SHOULD BE REGARDED AS A NOMINAL PARTY WHOSE CITIZENSHIP IS IMMATERIAL IN DETERMINING DIVERSITY JURISDICTION.

The stockholders' derivative action is an anomaly in the law. It is one to enforce a cause of action which the corpora-

tion itself might have sued to enforce, if unfettered, but must be unmixed with any cause of action which the complaining stockholder might have individually.

The position which the complaining stockholder occupies in a stockholders' derivative action has, by analogy, been defined in many different ways by the courts.

In *Koster v. Lumbermen's, supra,* this Court said:

> "The cause of action which such a plaintiff brings before the court is not his own, but the corporation's. It is the real party in interest and he is allowed to act in protection of its interest, somewhat as a 'next friend' might do for an individual because it is disabled from protecting itself."

In "next friend" suits in federal courts, it has always been held that it is the citizenship of the "infant" and not that of the "next friend" which determines diversity for the purpose of federal jurisdiction.

Voss v. Neineber, 68 F 947;
Blumenthal v. Craig, (CCA) 81 F. 320

In *Kohler v. McClellan, (D.C. La.) 77 F. Supp. 308, 314,* the court classifies the stockholder as a "nominal plaintiff"; *Denike v. Anglo California Nat. Bank, (CCA 9) 145 F. (2d) 285, 289 (4, 5)* assimilates his position to that of a "guardian ad litem"; *Chaplin v. Selznick, 293 N.Y. 529, 532, 58 N. E. (2d) 719, 720,* classifies him as "the nominal plaintiff *** the instigator" of the action. *Pomeroy on Equity Jurisprudence, 4th, Ed. 1095,* says the stockholder:

> "is permitted to sue in this way simply in order to set in motion the judicial machinery of the court."

The plaintiff-stockholder in a stockholders' derivative action is at most only a nominal plaintiff. He has no direct interest in the controversy different from that of all of the stockholders. The cause of action belongs to the corporate

body and not to the plaintiff and other stockholders individually, not even to the body of stockholders collectively. The judgment inures to the corporation as a separate entity, and all consequential benefits belong to all its stockholders.

Section 567, verbo Corporation, 18 Corpus Juris Secundum, p. 1288, in part, reads:

> "A suit by a stockholder on behalf of the corporation must be brought in equity. The suit is for the benefit of the corporation and all stockholders, and the real controversy is between the corporation and the persons whose acts are complained of, the corporation being the beneficial plaintiff."

The decision of the Court of Appeals is in conflict with the decision of this Court in *Stewart v. B. & O. Railroad Co., 168 U.S. 445, 459,* an action brought for the benefit of another, where this Court held:

> "For purposes of jurisdiction in the Federal courts regard is had to the real rather than to the nominal party."

The decision of the Court of Appeals is in direct conflict with the decision of this Court in *Bush v. Elliott, 202 U.S. 477,* which was a derivative action brought by plaintiffs as bankruptcy trustees in the Circuit Court for the Northern District of Alabama. One of the trustees was a citizen of Alabama and the two defendants were citizens of the same state. The bankrupt was a New Jersey corporate citizen. Diversity jurisdiction was upheld, because the trustees sued in the right of the bankrupt, whose citizenship was held to control upon the question of diversity. The statute involved was *Section 23(b) of the Bankruptcy Act as amended, Section 46(b), 11 U.S.C.A.* There is a more logical reason for holding in this action that the injured corporation's citizenship determines jurisdiction of the controversy here, than, that the bankrupt's citizenship controlled in *Bush v. Elliott, supra,*

where the legal title to the claims asserted on behalf of the bankrupt had vested in the trustees. The legal title to the claims asserted on behalf of Crescent are in Crescent, and have not vested in the stockholders, either individually or collectively.

In *Walden v. Skinner, 101 U.S. 577, 589,* this Court, citing *Arapahoe County v. Kansas Pacific Ry. Co., supra,* said;

> "Cases arise in the Federal courts in which nominal or even immaterial parties are joined, on the one side, or the other, with those who have the requisite citizenship to give the court jurisdiction of the case, and where that is so, the rule is that the mere fact that one or more of such parties reside in the same state with one of the actual parties to the controversy will not defeat the jurisdiction of the court."

Mrs. Tucker, the stockholder plaintiff, having no individual controversy with any of the named defendants, including Crescent ,and not being entitled to any individual relief—under the allegations of the complaint, her position is that of a nominal plaintiff, and her citizenship does not defeat the jurisdiction of federal courts of the controversy between citizens of different States set out in the complaint. The Court of Appeals erred in affirming the judgment of the District Court holding to the contrary.

III.

THE POSITION OF AN INJURED CORPORATION IN A STOCKHOLDERS' DERIVATIVE ACTION CAN NOT BE FIXED AS THAT OF A REAL DEFENDANT BECAUSE IT IS IN THE ANTAGONISTIC HANDS OF THE MAJORITY DIRECTORS AND STOCKHOLDERS WHOSE FRAUD IS THE ESSENCE OF THE ACTION.

Crescent, the injured corporation, filed no pleadings in this action. Irrespective of that fact, both lower courts held, in effect, that Crescent's position in the action was fixed as

being adverse to the enforcement of its own claims against its wrongdoers—because the wrongdoers were antagonistic.

Modern decisions, both Federal and State, are unanimous in holding that the injured corporation, in a stockholders' derivative action, can take no position which is fundamentally antagonistic to the claims asserted on its behalf, where fraud of the majority directors and stockholders is the essence of the stockholders' derivative action.

This question has not been, but should be, decided by this Court, since its decision is important to the jurisdiction of federal courts in wide areas of litigation.

In *Otis & Co., v. Pennsylvania R. Co (D. C. Pa.) 57 F. Supp. 680, 684,* the Court said:

> "The stockholders' action is critical of the corporation's management and the corporation should have a right to answer subject to the exceptions hereinbefore mentioned, where fraud of the directors or management is the essence of the stockholders' action."

In *Meyers v. Smith, (1933) 190 Minn. 157, 251 N. W. 20,* a stockholder sued, on behalf of his corporation, to recover money claimed to have been misappropriated by certain of its directors out of corporate funds. The corporation filed an answer containing affirmative defenses to the charges against its directors. In striking the corporation's answer, the court said (page 21 of 251 N. W.):

> "The corporation is a nominal party. It was properly joined as a party for the protection of the defendants, so that when final judgment is entered the two individual defendants may be thereby protected from a second suit on the same cause of action by the corporation. *** But that does not vest in the corporation the right to here step in and, by answer, attempt to defeat what is practically its own suit and cause of action."

Slutzker v. Reiber, (1942), 132 N. J. Eq. 412, 28 A. (2d) 258, is to the same effect, the court denominating the injured

corporation as a *formal* defendant, and the wrongdoers as *actual* defendants.

In *Chaplin v. Selznick, (1945), 58 N. Y. S. (2d) 453, the* injured corporation, United Artists, had associated itself with the defendant by denying the allegations of the complaint and asking for its dismissal. After reviewing many cases dealing with the theory of stockholders' derivative actions, both English and American, the court defined the position of the corporation on page 455, as follows:

> "*Here we must distinguish between the corporation as a separate entity and the management, of the corporation.* The management, the board of directors, may take a position antagonistic to a claim asserted on behalf of the corporation. That antagonistic position gives a stockholder the right to take the matter out of the hands of the management and to bring his action in a representative capacity on behalf of the corporation. *The corporation itself can take no position in a derivative stockholders' suit which is fundamentally antagonistic to the claim asserted on its behalf.* That is the whole theory which is behind a derivative stockholders' action." (Emphasis supplied)

If the injured corporation itself is forbidden by law and the principles of equity to take a position fundamentally antagonistic to the claims asserted on its behalf in a stockholders' derivative action, by what system of judicial legerdemain may such position be imputed to it?

The refusal of the lower courts to realign Crescent as a complainant in this action, where its interest lies and as required by law, was based upon the untenable position that it could not be so realigned because it was in antagonistic hands. This demands a reversal of the judgment of the Court of Appeals.

PUBLIC IMPORTANCE OF THE ISSUES.

The issues here involved are of great public importance, affecting as they do the jurisdictional integrity of federal courts in wide areas of litigation. The reports of federal decisions contain many cases involving frauds upon corporations by persons whose citizenship is diverse from the citizenship of the corporation, and which may be redressed only through the medium of a stockholders' derivative action in the federal courts.

The public policy of the United States as repeatedly expressed by this Court, as well as the public policy of all of the States, requires the faithful discharge of duties by persons holding positions of trust and confidence. Courts have ever been jealous to assert and enforce the public policy that no man can serve two masters by manipulating his position as trustee in his own interest. Whenever it has been made to appear that transactions have occurred in which a trustee was dealing with himself, the overwhelming majority of the courts have been intent on finding ways to defeat, rather than sustain, such transactions.

It is universally held that contracts and acts against such public policy cannot be made valid by ratification, and are illegal and void, as tending to be, or being, a fraud on third persons.

The Constitution confers jurisdiction upon federal courts of controversies between citizens of different States. Whenever such a controversy is presented to a district court above the amount specified by *Section 1332, supra,* and the parties to such controversy are properly before the court, it is the court's duty to assume jurisdiction. To correctly determine diversity jurisdiction, it is necessary for the court to decide the nature of controversy, and the citizenship of the parties to that controversy.

Until the decision of the Court of Appeals in this case, no appellate court in the United States had ever held that the controversy in a stockholders' derivative action, which complained solely of fradulent breaches of trust on the part of its corporate managers and majority stockholders, was other than a controversy between the injured corporation and such alleged wrongdoers.

The decision of the Court of Appeals below has sanctioned the holding by the District Court that the controversy in such an action is one between the plaintiff-stockholder, on one side, and the injured corporation and the wrongdoers on the other. Such decision is contrary to and in conflict with the decision of the Second Circuit in *De Neufville v. New York & Northern Ry Co., supra,* and the decision of the Third Circuit in *Laughter v. Schell, supra,* which hold that the controversy in such cases is one between the corporation and the alleged wrongdoers.

The two decisions last mentioned, however, are in conflict with each other, as to whether the rule obligating federal courts to realign the parties for jurisdictional purposes according to their real interests in the controversy, is applicable in a stockholders' derivative action. The decision from the Second Circuit decided the rule to be inapplicable, while the decision from the Third Circuit held it applicable.

The decision of the Court of Appeals below is in accord with the *De Neufville Case, supra,* that the rule of realignment is not applicable in stockholders' derivative actions. The reasons assigned by each court for this conclusion are entirely different. Each of these two decisions claim authority for this view in decisions of this Court, which do not, as we have shown, support it.

Under no stretch of the imagination may it truthfully be said that any adverse interest exists between the complaining stockholder and her corporation in the case at bar. Nor is

there any justiciable controversy alleged or existing between Mrs. Tucker and her co-citizens of Louisiana. The complaint alleges facts which entitle her to represent her corporation in the prosecution of its claims to the exclusion of its unfaithful corporate managers.

It is of vital public importance that the questions presented be finally decided by this Court because such decision will affect the jurisdictional integrity of Federal courts of controversies between citizens of different States. The decision of the Court of Appeals in this case furnishes corporate managers complete civil immunity from having to account to their corporation for fraudulent breaches of trust, where they and their corporation are citizens of different States, and where all of the corporation's stockholders are citizens of the same state as the corporate managers. In such instances there is no State tribunal where the injured foreign corporation and its local unfaithful managers, the actual parties to a controversy thus arising, may be compelled to appear, because the process of a State can not run beyond its boundaries. Where the requisite statutory amount is in controversy the Federal courts should not deny to a corporate citizen of one State who has been defrauded by citizens of another State, the right to have its property protected through a representative action in its courts.

A corporate citizen is entitled to the protection of its property against fraudulent misappropriation by its managers upon the same basis as the property rights of individual citizens are accorded protection under the law. It is entitled to be represented by its stockholders in the prosecution of suits to protect its property rights on its behalf, to the same extent as one individual might act for an infant, lunatic, or other helpless individual. The mere fact that it is placed as defendant instead of plaintiff in a suit in chancery, never changes its relation to the matter in controversy. *Arapahoe County Case, supra, p. 285.*

CONCLUSION

The Petition for Certiorari should be granted in order that this Court may review the decision of the United States Court of Appeals for the Fifth Circuit in this case.

Respectfully submitted,

William G. McRae,

Richard A. Dowling,
Attorneys for
Mrs. Odile V. Hubert Tucker,
as a stockholder, on behalf of
Crescent City Laundries, Inc.
Petitioners.

IN THE

Supreme Court of the United States

October Term, 1951.

Office-Supreme Court, U. S.
FILED
SEP 6 1951
CHARLES ELMORE CROPLEY
CLERK

No. 210.

MRS. ODILE V. HUBERT TUCKER, as a Stockholder, on behalf of CRESCENT CITY LAUNDRIES, INC.,
Petitioners,

vs.

NEW ORLEANS LAUNDRIES, INC., *et al.*,
Respondents.

Brief in Opposition to Petition for a Writ of Certiorari.

ABNER GOLDSTONE,
SIDNEY A. WOLFF,
Attorneys for Respondent,
New Orleans Laundries, Inc.,
527 Fifth Avenue,
New York City, N. Y.

LEONARD B. LEVY,
EDWIN F. MARX,
Attorneys for Respondents, Charles Lob, Liquidator of Weil & Co., Inc.; Charles Lob and Walter H. Weil, Jr., Surviving Partners of Weil & Company; Succession of Walter H. Weil and Walter H. Weil Jr., Testamentary Executor of Walter H. Weil; George W. Robertson; Brent S. Robertson; Leonard B. Levy; Edwin F. Marx; Charles Lob; and Walter H. Weil, Jr.,
1006 National Bank of Commerce Building,
New Orleans, Louisiana.

LODER APPEAL PRESS, INC., 65-67 Duane St., N. Y. C., Tel. WOrth-2-0689

INDEX.

PAGE

Statement 1

Argument:

A long line of authorities establishes that in a stockholders derivative action, the citizenship of the complaining stockholder, and not of the allegedly wronged corporation, determines whether or not there is the requisite diversity of citizenship 2

Conclusion 7

TABLE OF CASES.

Dawson v. Columbia Trust Company, 1905, 197 U. S. 178, 181 4

DeNeufville v. New York & N. Ry. Co., 2 Cir., 1897, 81 Fed. 10 5

Doctor v. Harrington, 1905, 196 U. S. 579 ..... 3, 4, 5

Dodge v. Woolsey, 1856, 18 How. (59 U. S.) 331 ... 2, 5

Hamer v. New York Railways Co., 1917, 244 U. S. 266, 274 ..... 4, 5

Hawes v. Oakland, 1882, 104 U. S. 450 2

Helm v. Zarecor, 1911, 222 U. S. 32, 36 4

Indianapolis v. Chase National Bank, 1941, 314 U. S. 63 ..... 3, 4, 5

Koster v. (American) Lumbermens Mutual Casualty Co., 1947, 330 U. S. 518 3

Lavin v. Lavin, 2 Cir., 1950, 182 F. 2d 870, 871 4

Venner v. Great Northern Railway Company, 1908, 209 U. S. 24 3

Wathen v. Jackson Oil & Refining Company, 1915, 235 U. S. 635, 639 4

RULES OF PROCEDURE.

Equity Rule 27, 198 Fed. xxv 3

Equity Rule 94, 104 U. S. ix 3

Federal Rules of Civil Procedure, Rule 23 (b) 3

IN THE

Supreme Court of the United States

OCTOBER TERM, 1951.

MRS. ODILE V. HUBERT TUCKER, as a Stockholder, on behalf of CRESCENT CITY LAUNDRIES, INC., *Petitioners,* vs. NEW ORLEANS LAUNDRIES, INC., *et al.,* *Respondents.*	No. 210.

Brief in Opposition to Petition for a Writ of Certiorari.

Statement.

Plaintiff, as a stockholder of Crescent City Laundries, Inc., petitions this Court for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit, to review the record and judgment entered by that Court in this action on April 5th, 1951.

The error specified as the foundation for the petition is the affirmance by the Court of Appeals of the judgment of the District Court which dismissed this action because of a lack of diversity of citizenship between the plaintiff and all of the defendants.

A Long Line of Authorities Establishes That in a Stockholders Derivative Action, the Citizenship of the Complaining Stockholder, and Not of the Allegedly Wronged Corporation, Determines Whether or Not There Is the Requisite Diversity of Citizenship.

In seeking a review by this Court, petitioner contends that the question of proper realignment and classification of the parties for the purpose of determining diversity jurisdiction in a stockholders derivative suit is an open one (p. 5, her brief).

But petitioner errs. This Court has, time and time again, laid down the fundamental rule that in a case, such as the one at bar, the alleged wronged corporation, claimed to be in antagonistic hands, will not be realigned as a plaintiff for jurisdictional purposes.

This question was first considered by the Supreme Court in 1856 in *Dodge* v. *Woolsey,* 18 How. (59 U. S.) 331, where a Connecticut stockholder in an Ohio corporation sued to prevent Ohio taxing officials from collecting a tax from the corporation. Realignment was refused, the Court holding, page 346:

> "The papers in the case also show, that the directors and himself (the plaintiff stockholder) occupy antagonist grounds in respect to the controversy which their refusal to sue forced him to take in defence of his rights as a shareholder in the bank."

(Before a stockholder may maintain a derivative suit, he must allege that the management of the corporation is antagonistic to the interests of the stockholder and of the corporation. *Hawes* v. *Oakland,* 1882, 104 U. S. 450. The doctrine of this last cited case was subsequently codified

in Equity Rule 94, 104 U. S. ix, followed by Equity Rule 27, 198 Fed. xxv, and is now substantially embodied in Rule 23 (b), Federal Rules of Civil Procedure. Petitioner made the requisite allegations in her complaint [R. 222].)

The question of realignment in stockholders derivative suits was next considered by the Supreme Court in *Doctor* v. *Harrington*, 1905, 196 U. S. 579, where the Court refused to realign the wronged corporation as a plaintiff on the ground that the antagonism of the corporate officers toward the plaintiff justified the classification of the corporation as a defendant.

Again, in *Venner* v. *Great Northern Railway Company*, 1908, 209 U. S. 24, this Court, in a stockholders derivative suit, refused to realign as a party plaintiff a corporation which was in antagonistic hands.

Thereafter in 1941, the Supreme Court, in *Indianapolis* v. *Chase National Bank*, 314 U. S. 63, cited, among others, its prior decision in *Doctor* v. *Harrington*, supra, in support of the statement (p. 70):

> "These familiar doctrines governing the alignment of parties for the purposes of determining diversity of citizenship have consistently guided the lower federal courts and this Court."

Six years later, in *Koster* v. (*American*) *Lumbermens Mutual Casualty Co.*, 1947, 330 U. S. 518, the Court again considered the problem of federal jurisdiction based upon diversity of citizenship within the framework of derivative suits by stockholders; and in discussing the "complexities and unique features of these actions", the Supreme Court reaffirmed the doctrine of *Doctor* v. *Har-*

rington, according special treatment to such actions with the observation that "jurisdiction is saved in this class of cases by a special dispensation because the corporation is in antagonistic hands" (p. 523).

Although not in point on all issues, it is to be noted that the case of *Doctor* v. *Harrington* has been cited with approval by the Supreme Court in several other decisions, i. e.:

> *Dawson* v. *Columbia Trust Company,* 1905, 197 U. S. 178, 181;
> *Helm* v. *Zarecor,* 1911, 222 U. S. 32, 36;
> *Wathen* v. *Jackson Oil & Refining Company,* 1915, 235 U. S. 635, 639;
> *Hamer* v. *New York Railways Co.,* 1917, 244 U. S. 266, 274.

It therefore appears clear that the petitioner errs in suggesting that this case presents "new questions"; rather, she is seeking to have this Court change the "familiar doctrines governing the alignment of parties for the purposes of determining diversity of citizenship" (*Indianapolis* v. *Chase National Bank,* supra). But as Chief Judge Learned Hand said in refusing to realign parties in the recent stockholders derivative suit of *Lavin* v. *Lavin,* 2 Cir., 1950, 182 F. 2d 870, 871, the Supreme Court:

> "has shown no disposition to change the rule in *Doctor* v. *Harrington,* 196 U. S. 579, 25 S. Ct. 355, 49 L. Ed. 606, but has recognized its continued authority."

An analysis of the cases cited by the petitioner reveals a number of them did not involve stockholders derivative suits, and hence can have no application to the issue presented.

The remaining cases cited by petitioner—those which involved stockholders derivative suits—indicate in both theory and result a uniform application of the rule of *Dodge* v. *Woolsey* and *Doctor* v. *Harrington*.

For example, in *DeNeufville* v. *New York & N. Ry. Co.*, 2 Cir., 1897, 81 Fed. 10 (pp. 6, 14, 20, 34, petitioner's brief), it was held that the corporation could not be realigned as a complainant since it was under antagonistic control.

And in *Hamer* v. *New York Railways Co.*, 1917, 244 U. S. 266, 274 (pp. 7, 14, 15, 23, petitioner's brief), the Court again approved the doctrine laid down in *Doctor* v. *Harrington*, and distinguished the *Hamer* case on its facts from a stockholders derivative action against a corporation in antagonistic hands.

In the light of the long line of authorities and the settled practice, the case at bar presents no "new questions with respect to diversity jurisdiction of the Federal Courts" as claimed by petitioner (p. 5, her brief).

In effect, petitioner seeks to have this Court expand the doctrine of diversity of citizenship beyond its present limits. That plaintiff herself may not be in a position to establish diversity of citizenship is no reason for enlarging the Court's jurisdiction and changing well settled rules. If diversity jurisdiction is to be enlarged, it is for Congress. Appropriate on this is the language of this Court in *Indianapolis* v. *Chase National Bank, supra*:

> " * * * The fact that Chase prefers the adjudication of its claims by the federal court is certainly no reason why we should deny the plain facts of the controversy and yield to illusive artifices. Settled restrictions against bringing local disputes into federal courts cannot thus be circumvented.

These requirements, however technical seeming, must be viewed in the perspective of the constitutional limitation upon the judicial power of the federal courts, and of the Judiciary Acts in defining the authority of the federal courts when they sit, in effect, as state courts (citing cases). The dominant note in the successive enactments of Congress relating to diversity jurisdiction, is one of jealous restriction, of avoiding offense to state sensitiveness, and of relieving the federal courts of the overwhelming burden of 'business that intrinsically belongs to the state courts,' in order to keep them free for their distinctly federal business (citing cases).

'The policy of the statute (conferring diversity jurisdiction upon the district courts) calls for its strict construction. The power reserved to the states, under the Constitution, to provide for the determination of controversies in their courts may be restricted only by the action of Congress in conformity to the judiciary sections of the Constitution. * * * Due regard for the rightful independence of state governments, which should actuate federal courts, requires that they scrupulously confine their own jurisdiction to the precise limits which the statute has defined.' *Healy* v. *Ratta,* * * * (292 U. S. 263, 270) * * *. In defining the boundaries of diversity jurisdiction, this Court must be mindful of this guiding Congressional policy * * * (citing cases) * * * *" (pp. 76-7).

CONCLUSION.

The Petition Should Be Denied.

Respectfully submitted,

ABNER GOLDSTONE,
SIDNEY A. WOLFF,
Attorneys for Respondent,
New Orleans Laundries, Inc.

GOLDSTONE & WOLFF,
Of Counsel.

JOSEPH KAROW,
MAURICE S. SPANBOCK,
On the Brief.

LEONARD B. LEVY,
EDWIN F. MARX,
Attorneys for Respondents, Charles Lob, Liquidator of Weil & Co., Inc.; Charles Lob and Walter H. Weil, Jr., Surviving Partners of Weil & Company; Succession of Walter H. Weil and Walter H. Weil Jr., Testamentary Executor of Walter H. Weil; George W. Robertson; Brent S. Robertson; Leonard B. Levy; Edwin F. Marx; Charles Lob; and Walter H. Weil, Jr.,

DUFOUR, ST. PAUL & LEVY,
Of Counsel.

Certificate as to Service.

I, the undersigned, do hereby certify that I have this day served a copy of the foregoing brief on each of the attorneys for the petitioner by depositing the same in the United States mail, postage prepaid, at New York City, New York, addressed to said attorneys at their respective post office addresses.

September 4, 1951.

SIDNEY A. WOLFF.